

## COMMENTARY

By David Greising

### WHEN BANKS ACT LIKE BROKERS, WHO REGULATES?

**T**he abusive atmosphere at the securities division of NationsBank Corp. in the early 1990s was shocking even for veteran stockbrokers. Working at the bank's branches, several recalled, they were told to hawk NationsBank's investment products to bank customers without explaining that they were brokers, not bankers. When elderly customers came in to roll over jumbo certificates of deposit, bank tellers got a cut of the commissions for turning them over to brokers who sold them NationsSecurities' risky closed-end bond funds instead.

When NationsSecurities' brokers complained to their bosses, say ex-employees, they got the brush-off. According to the ex-brokers, Charles King, then executive vice-president of NationsSecurities, told them to keep selling; sales targets would be raised, he warned, not lowered. Meanwhile, the main fund they were hawking, Nations Term Trust 2003, lost 35% of its value in just seven months, in part because of investments in risky derivatives. They later regained the losses.

When BUSINESS WEEK first reported the troubles at NationsSecurities nearly four years ago, NationsBank,

paid to settle class actions in two customer and administrative complaints in Florida, Texas, and South Carolina.

But let's not cheer regulators for their aggressive enforcement just yet. The bank got off easy. Our balkanized regulatory system's rules would have made it difficult to hold personally responsible top bank executives such as CEO Hugh L. McColl Jr. and other officials for a bank's misdeeds. The case

from Beltway-speak, that means bank divisions that act like brokerage firms would be regulated as brokerage firms.

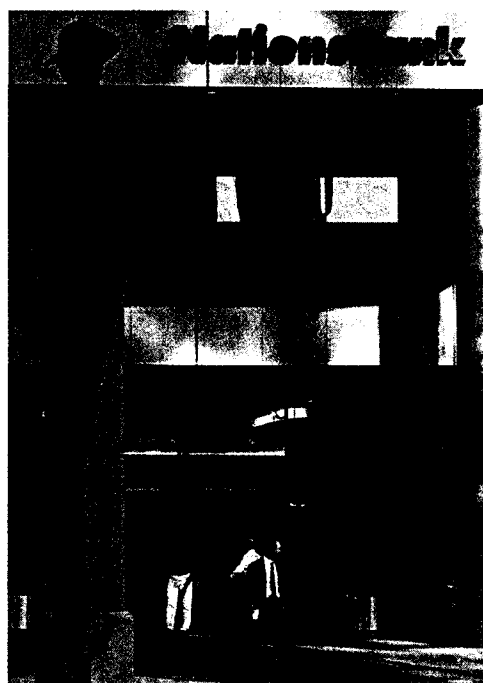
It's an idea whose time is long overdue. Banks have pushed to stay under the umbrella of banking regulators, who have precious little experience with brokerage derring-do. But in an era when every ambitious bank is copying the playbook of Merrill

Lynch & Co., not J.P. Morgan & Co., that's a recipe for regulatory oversight. It leaves regulators unable to stop sleazy selling practices by stockbrokers dressed in bankers' pinstripes. Paul V. Gerlach, associate director for enforcement at the SEC, says misdeeds like those at NationsSecurities "are not an isolated problem." And the SEC has a hard time cracking down because banks "are not subject to the full panoply of securities laws."

**INTIMIDATING.** The challenges for regulators grow more daunting as banking-industry consolidation accelerates. Given its proposed merger with BankAmerica Corp., NationsBank is set to become one of the country's largest brokerage firms. The pending merger of Travelers Group and Citicorp would bring the entire Salomon

Smith Barney operation under the umbrella of banking regulators. Other big banks have already acquired their own brokerages or are expected to do so soon. David Cray, a former NationsSecurities broker, now an independent broker, who first brought charges against the firm four years ago, frets that big banks intimidate regulators. "Any one agency alone can be frightened of an institution as large and powerful as NationsBank," Cray says. But if regulatory reforms cause all the agencies to work together, they might have the clout to frighten even the giants like NationsBank.

*Greising covers banking from Atlanta. Paula Dwyer in Washington contributed additional reporting.*



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#### DESPITE PAYING \$6.75 MILLION, THE BANK GOT OFF EASY

based in Charlotte, N. C., denied any improper sales practices and said it had no problem with procedures at NationsSecurities. But on May 4, the bank forked over \$6.75 million to settle administrative proceedings without admitting or denying allegations of misleading sales practices brought by banking and securities regulators. King and two other bank officials personally were fined and suspended as brokers for up to six months. King could not be reached for comment. The bank says the settlement "puts the issue behind us."

Those fines come on top of more than \$60 million NationsBank has

shows how difficult it is to regulate stockbrokers working for banks, in part because bank regulators usually lack the skills or the inclination to root out securities fraud.

The timing of the NationsBank settlement may prove opportune, though. It could add much-needed weight to calls for reform as Congress, starting this month, considers a bill to modernize banking regulation. As part of an effort to bring Representative John D. Dingell (D-Mich.) on board, Republicans have agreed to accept a series of amendments that would strengthen "functional" regulation of financial services. Translated